

NEXO



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REVITALIZING MICHIGAN'S ECONOMY THROUGH MINORITY-OWNED SMALL BUSINESSES

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"Our Nation's economic growth and ability to compete in the international marketplace depends on the full participation of all members of our society. Minority businessmen and women have helped to expand our economy through innovation, hard work, by taking advantage of the opportunities available in our free market systems. These entrepreneurs have become an indispensable force in our economy and they will continue to play a key role in our efforts to expand America's share of world markets"

(George Bush, 1989.)

Introduction

The decline of the U.S. economy has been a source of concern and debate among many scholars, politicians and citizens. Many people have questions concerning the current state of our economy and the high levels of persistent unemployment. When did this happen? How did this happen? Who is to blame? What can be done to help spur economic growth?

The origin of the economic recession in the United States remains a source of debate. Although the recession was officially recognized in December of 2007, many, including those in the Federal Reserve, point to the last trimester of 2006 as its starting point, while others point to start of that decade and the policies of the Bush Administration as leading to the recession. In reality, although it is impossible to pinpoint the exact point at which it all went wrong, the Center



for American Progress examined the shift from a Federal budget surplus to a \$6 trillion deficit and points to a nexus of causes, including the Bush Tax Cuts of 2001-2008, increased military spending, especially the funding of the wars in Iraq and Afghanistan, Medicare increases, domestic spending, and the stimulus package of the Obama administration.

These spending policies, however, were only one factor contributing to the "The Great Recession." Two other factors played a huge role in the economic downfall: the housing crisis and the credit crisis. In regards to the housing crisis there has been a tendency to blame loans to minorities and low-income citizens: 1) The Community Reinvestment Act forced lenders into extending loans to low-income households and businesses who were unable to repay;

2) Lenders were forced into offering loans to minorities in order to increase homeownership by minorities. These arguments do not hold water, however. "According to the Federal Reserve Board, only 6% of high-cost subprime loans to low and moderate-income households were originated by banks subject to CRA regulation . . . and less than 10% of subprime loans were for first-time ownership" (Carr, 2010, p. xix). Whatever the causes of the housing and credit crises, the fact remains that minorities have been disproportionately affected by the recession. In June of 2009, unemployment was at a shocking 9.5% nationally; however, the rate was even higher for minorities: 15% for African Americans and almost 12% for Latinos (Carr, 2010).

In Michigan, the hardships stemming from the dip in the US economy have been even more marked. In 2009, when the unemployment rate was at 9.5% nationally, the unemployment rate in Michigan was at 14.1%. Recently however, this rate has begun to drop as the automotive industry has experienced some recovery, contributing to the creation of 67,000 jobs in 2011. This, however, is not the entire story; another segment is based on the fact that the labor force in Michigan has dropped by 4.6% (Luhby, 2012). In this context, job creation in Michigan must continue to be a critical concern of economic growth. Furthermore, recognition of the racial diversity of the state and the disproportionate effects of economic hardships felt by minorities requires the development of targeted policies to address this problem.

Race and the Economy

Last year, President Obama was re-elected as President and became the first president in our history to be elected without a majority of the White vote (Kogan, 2012). Although many argue that as a society, we have progressed past our racial history, institutional racism still exists within our system. As a society, we must not become complacent with our progress in race relations up to this point; rather, we must continue to strive to combat racism in institutional practices in order to achieve both social justice and racial justice within the United States (powell & Reece, 2010:19).

As indicated above, many of economic and social problems faced by low-income communities are symptomatic of and rooted in disproportionately high levels of unemployment and underemployment. According to the Bureau of Labor Statistics (2012), the Hispanic unemployment rate was at 10% in October of 2012, which was well above the national average of 7.9%; Michigan too was above the national average at 9.3% that month. Furthermore, labor statistics show that while unemployment rates for all racial and ethnic groups generally tend to be directly proportional to the GDP of the country, race and ethnic minorities tend to have consistently higher unemployment rates than Whites. Although Latinos have begun to increase their employment rates, and in some places throughout the country have actually been either equal to or higher than that of White, the racial disparity can be seen in the wage gap which continues to grow. In fact, data from the Bureau of Labor Statistics show that from 1973 to 2007, Whites had about a 40% wage advantage over Latinos and this wage gap has been increasing since 1989 (Foster-Bey, 2010).

The fact that minorities have grown into a powerful social and political groups cannot be ignored. It is generally noted that minorities turned out to vote in record-breaking numbers, with 71% of voting Latinos having voted for Obama. As the minority vote continues to grow, politicians cannot push the disproportionate effects of the current state of the economy on minorities to the background. Job creation and job growth must continue to be of utmost importance in order to provide a better quality life for minorities across the nation and in Michigan (Mosbergen, 2012).

Growth through Small Business

Developing a workforce and creating jobs within a community can help address the unemployment problem. One way to promote job growth within Michigan is to provide more assistance to small businesses within the state. Small businesses are an important source of job growth, help strengthen the overall economy through innovation and flexibility, and contribute to the sustainability of community and

neighborhood economic development (Lohrentz, 2010). The U.S. Small Business Administration has four qualifications for being recognized as a small business: 1) Independently owned and operated, 2) For-profit organization status, 3) Is not dominant in its field, and 4) is limited in size. In a context in which large-scale manufacturing declined through out-migration, in the period from 1996 through 2005, small businesses accounted for approximately 50 percent of private sector employees and from 60 to 80% of new jobs (Lohrentz, 2010).

The Advantages of Minority-Owned Small Businesses

Businesses owned by women and minorities are sources of job growth within a community. These businesses are more likely to hire other minorities and women (Lohrentz, 2010). As discussed above, minorities, on average, have higher unemployment rates than Whites. By promoting small businesses among minorities, who are more likely than others to hire more minorities, growth in the overall economy, reduction of the wage gap, and growth of the labor force can be perpetuated while lowering minority unemployment rates. Furthermore, minority-owned businesses promote investment and reinvestment in “vulnerable” communities and can provide a source of tax revenue for local governments (Lohrentz, 2010).

Barriers Faced by Small Businesses

In *Building Healthy Communities* (2010), Tim Lohrentz notes and analyzes many of the barriers which small businesses must overcome in order to be successful. These include isolation within the economy, community barriers, limited owner education, licensing and regulation problems, health insurance costs, and lack of financing.

Many of these factors contain a racial bias. For example, it is commonly known that African American and Latino populations, on average, have lower education levels than Whites, with Latinos being the least likely to be college graduates. Furthermore, this lack of education leads to many difficulties in understanding and complying with the licensing and regulation requirements set forth by both the federal and

state governments (Lohrentz, 2010).

Aside from race-based factors, small businesses are subjected to many costs which hinder their success. For example, transaction costs which are not cumbersome to large corporations and companies can be extremely cumbersome for a small business (Bushaw, 2001). Furthermore, large firms are able to rely on their reputations to attract business, and investors often require proof of the credibility of firms in which they are investing. This provides a problem for small businesses which are just starting up. Competing in a larger market is incredibly difficult for small businesses. “With high transaction costs, inadequate access to capital and product markets, deficient training, and insufficient infrastructure, one wonders how any small business is able to set up shop, must less survive or prosper” (Bushaw, 2001, p. 225).



Helping Minority-Owned Small Businesses Through Federal Means

Despite the many barriers to establishing and owning a successful small business, they continue to grow as part of our economy. The Federal Government has recognized the importance of small businesses to the economy and has implemented several policies and legislation which have helped to increase the success of small businesses across the country. These include the Small Business Jobs and Credit Act, the Community Reinvestment Act, the New Markets Tax Credit, and other programs. These programs work generally by providing financing to small businesses. For example, the Small Business Jobs and Credit Act of 2010 was enacted to help provide credit options for small businesses

which had been drastically affected by the Great Recession (Gerwin, 2011). Signed into law by President Obama in 2010, the Small Business Jobs and Credit Act includes provisions on credit access, loans, tax incentives, and tax breaks.

Affirmative Action at the National Level

Federal programs that are specifically designed to help minority-owned businesses have faced increasing roadblocks as threats to Affirmative Action policies have continued to increase. Affirmative Action policies are designed to provide opportunities for minority groups that historically have been the targets of discrimination. Affirmative Action policies have been implemented across the country since the 1960s. In the business sector they call for “set aside” for minority businesses. However, these programs have been increasingly attacked as violating the equal protections clause of the 14th Amendment. In regards to this argument, two views emerge:

The ABA maintains that although equal opportunity is not yet a reality for many minorities and women, the significant gains that have been made during the past 30 years are clearly attributable in large part to effective affirmative action programs at both governmental and private levels.” Congress claims that “affirmative action is no longer needed and that these programs have promoted women and minorities at the expense of more qualified Caucasian males (DiLiberto, 1997:2039, footnote 6).

Because of these concerns, many cases have been argued before the Supreme Court of the United States in order to determine where affirmative action fits into today’s society. Three leading cases on the matter are *Fullilove v. Klutznick*, 448 U.S. 448 (1980), *City of Richmond v. J.A. Croson Co.* 488 U.S. 469 (1989), and *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200 (1995). These cases establish a strict scrutiny standard for enacting Affirmative Action policies and programs at the federal level. The strict scrutiny test requires that a policy or program have a compelling state interest and be narrowly tailored to meet that interest.

Fullilove v. Klutznick, 448 U.S. 448 (1980)

In this case, the U.S. Supreme Court examined the issue of set aside programs, specifically in regards to the Public Works Employment Act of 1977. The Act provided that minority contractors receive 10% of federal grant money designated to public construction projects (*Fullilove v. Klutznick*, 1980). Suit was filed arguing that this was a violation of the Equal Protection Clause provided in the Fifth Amendment of the Constitution. In that case, the Court determined that the Act was constitutional by applying a two part test: 1) Whether the purpose of the Act was within Congress’s power, and 2) Whether the purpose of the act was implemented by constitutional means (*Fullilove v. Klutznick*, 1980). The Court stated that the Act was implemented to rectify a history of discrimination and to provide for the general welfare, and that this was well within Congress’s power to do (*Fullilove v. Klutznick*, 1980).

City of Richmond v. J.A. Croson Co.(1989)

Set aside provisions were further examined in this case in which the J.A. Croson Company bid on a plumbing job in the City of Richmond, which at that time had implemented a “Minority Business Utilization Plan” in which all public construction contracts were required to subcontract 30% of the work to minority contractors. Croson was denied a waiver, lost the contract, and brought suit stating that the Minority Business Utilization Plan violated the 14th Amendment of the Constitution (*City of Richmond v. J.A. Croson Co.*, 1989). In this case, the Court implemented a strict scrutiny standard for all Affirmative Action programs, and stated that the Plan did not provide a “compelling government interest” and was not narrowly tailored. Further, the Court stated that a city cannot rely on societal discrimination as the basis for providing relief to historically disadvantaged groups, but rather must point to specific evidence of discrimination (*City of Richmond v. J.A. Croson Co.*, 1989).

Adarand Constructs, Inc. v. Peña (1995)

In this case, the Supreme Court once again reviewed set aside and Affirmative Action programs in regard to construction contracts

and held that strict scrutiny is required for such federal programs. In *Adarand*, the Court reviewed a Department of Transportation policy which gave financial incentive bonuses to contractors who employed minority subcontractors. In this case, the Court held that strict scrutiny was the correct standard of review for affirmative action policies (*Adarand Constructors, Inc. v. Peña*, 515 U.S. 200, 1995).

Affirmative Action at the State Level

At the federal level, the cases summarized and described above provide a strict scrutiny standard that federal programs and policies must follow. However, what does this mean on a state level? What can be done on a state level in order to address the need for growth in the minority small business sector? “The workforce development system in most locations mirrors the federal system – it is a highly fragmented set of programs, policies, and institutions that are often ineffective at bringing labor supply and labor demand together (Foster-Bey, 2010, p. 265).” However, many states and cities have implemented policies and procedures meant to help spur job creation and growth through small business. By establishing programs at state and local levels, assistance to minority-owned and other small businesses can be tailored specifically to meet the needs of a local community. Furthermore, local communities and governments have the advantage of knowing specifically what a community needs, and what programs should be implemented in order to help small businesses. Furthermore, local initiatives are likely to be more successful at combating institutional racism within a community than are federal programs, which are sometimes aimed at recovery, but which are not likely to cover specific situations or loopholes which may be present within at the community level. The following section outlines some of these programs and follows their progress up until this point.

State and Local Policies and Programs

The Cincinnati Project

“Founded in the wake of Cincinnati’s 2001 race-related riots, the Cincinnati Minority Business Accelerator (MBA) was initiated by the regional chamber of commerce to address

major economic disparities in African American business and entrepreneurship” (Powell & Reece, 2010, p. 44). At that time, Cincinnati had a population which was approximately 40% African American, yet accounted for only 2% of the local business and entrepreneurial revenue (Powell & Reece, 2010). The Cincinnati MBA prepares minority businesses to be competitive in the business market. The program partners with larger businesses in the area (including Fortune 500 companies) to encourage minority businesses, assisting them develop business strategies, and promoting joint ventures. The pilot campaign program resulted in over \$200 million “in procurement commitments from 15 companies headquartered or operating in the Cincinnati region.” (Powell & Reece, 2010:44).

Massachusetts’ Early Care and Education

Massachusetts created an agency to regulate what is known as “Early Care and Education Programs” (Powell & Reece, 2010:45). These programs provide head start services and after-school care services for families in need. The goals of this agency are as follows:

- *To develop a statewide system of professional development for the early education and care of out of school time workforce, a critical element in improving the quality of care provided to families in the Commonwealth; and*
- *To oversee the creation of a groundbreaking program of voluntary, universally accessible high quality early childhood education for all preschool-aged children in the Commonwealth (Wohl, 2010:282).*

One might ask what this has to do with job creation and small businesses. By providing childcare benefits to families in need the workforce is freed up and parents have more time to create and operate small businesses. Furthermore, as noted earlier, one major barrier to minority-owned small businesses is the lack of education. By providing these services, states are contributing to the ability of the workforce to return to school in order to gain higher levels of education, and thus, to better prepare them to be business owners.

The Tennessee Small Business Investment Company Credit Act

Another program aimed at helping

small businesses succeed was recently enacted in Tennessee. In 2009, Tennessee enacted the Tennessee Small Business Investment Company Credit Act in order to help finance small businesses which are not able to secure financing in the traditional sense due to the economic downturn. The Tennessee General Assembly noted that loans to small businesses had decreased by 57% in some areas, and that “access to capital is critical for business startups, expansions, and more importantly, to the health of state and local economies (Krumm, 1993:93).

Other Examples

Other individual companies are also helping to address the disadvantages faced by minority small business owners within states. For example, President Obama recently commended Rising Tide Capital, Inc., in New Jersey, which helps minorities, women and other disadvantaged groups start and maintain successful businesses within disadvantaged communities (risingtidecapital.org). According to the Association for Enterprise Opportunity, microenterprise is defined as “any type of small business that has fewer than five employees and is small enough to benefit from loans of under \$35,000” (Jones & Spratley, 2010:380). Micro enterprises can serve as a way for people to begin to gain control of their financial situation and gain a better life for themselves.

In Oregon, where there is a sizeable population of Native Americans, the Oregon Native American Business and Entrepreneurial Network (ONABEN) is “a publicly supported nongovernmental organization designed to encourage the growth of small businesses owned by American Indians” (Bushaw, 2001:231). This organization acts as a liaison between federal and tribal governments and their resources, and also offers a network of programs, including training, information centers, financial counseling, and other business services” (Bushaw, 2001:232). ONABEN recognizes that the culture of a community or of a certain group of people can engender barriers that make it difficult for those unfamiliar with the local community or culture to address effectively (Bushaw, 2001).

These policies and programs are just a

few of the many ways by which states and local communities and businesses have taken control and are addressing the disadvantages that minority businesses face through institutional bias, poverty, education, and geographic disadvantages. In the future, these programs will likely continue to expand. Unlike federal programs aimed at federal contracts and small business growth of minority small businesses, privately owned businesses are not subject to the strict scrutiny standard employed by the Supreme Court. Moreover, many states including California, Nebraska, and Washington have bans on affirmative action policies, making them even more strict than federal standards (Lewin, 2011). These approaches require vision, will, and commitment on the part of local government and business leaders to address the development and incorporation of minority businesses into the economic mainstream.

Michigan's Support of Minority Businesses

So where is Michigan when it comes to supporting minority businesses? What legislative policies has Michigan implemented in order to address the institutional bias and high minority unemployment rate? Are these measures really necessary in Michigan? The answer to that question is yes. According to data released by the Kaiser Foundation (2011), Latinos account for approximately 5% of Michigan's total population. According to the Bureau of Labor Statistics (2012), in October of 2012, the Latino unemployment rate was at 10%, which was well above the national average of 7.9%, and Michigan itself was above the national average at 9.3%. Job creation and job growth must continue to be of utmost importance in order to provide a better quality life for minorities in Michigan.

The Michigan legislature has recognized the importance of small businesses within the economy and community, and has in recent years implemented public policies which promote small businesses and create jobs. According to Fowler: The Small Business Association of Michigan believes that the state's restructuring is producing the intended results. At the top of the list is the Legislature's elimination of the Michigan Business Tax, which not only reduced the tax burden on

small businesses, but also simplified the process by creating a flat rate of 6% for most corporate entities, minimizing costly and time consuming tax return preparation (Fowler, 2012).

Other policies recently implemented include reducing unemployment benefits (which were a burden on small businesses) and regulations on workers compensation (also borne by small businesses)(Fowler, 2012). However, although these changes have positively affected the small business sector, it is important to remember that sometimes changes like these can hurt the workers themselves and can also serve to promote the exploitation of the workforce. For these reasons, changes such as these are not always positive, and we must constantly remind ourselves that the need to promote small business growth must be balanced against the health and wellbeing of the workers employees within these small business entities.

Michigan and Affirmative Action

With regard to Michigan's stance on affirmative action policies, and whether or not such laws are allowed or are as restrictive as required by the Supreme Court in federal contract cases, in July of 2011, the Sixth Circuit overturned Michigan's ban on Affirmative Action passed in November of 2006. The Court held that Michigan's referendum, which amended Michigan's Constitution and "prohibited public institutions from giving "preferential treatment to any individual or group on the basis of race, sex, color, ethnicity or national origin," was unconstitutional with regard to governmental hiring and public university admissions" (Lewin, 2011).

In *Coalition to Defend Affirmative Action v. Regents of the University of Michigan*, 652 F.3d 607, 610-611 (6th Cir. Mich. 2011), the Sixth Circuit Court reviewed two Supreme Court cases [*Washington v. Seattle Sch. Dist. No. 1*, 458 U.S. 457, 102 S. Ct. 3187, 73 L. Ed. 2d 896 (1982); *Hunter v. Erickson*, 393 U.S. 385, 89 S. Ct. 557, 21 L. Ed. 2D 616 (1969)] in considering whether Proposal 2 (Michigan's ban on affirmative action in public universities and state government) was constitutional under the Fourteenth Amendment's Equal Protection Clause. The

Court held that Proposal 2 was unconstitutional in that it "alters Michigan's political structure by impermissible burdening racial minorities. This case effectively not only overturned the ban on affirmative action in Michigan, but is also "binding on Kentucky, Michigan, Ohio and Tennessee" (Lewin, 2011).

The Sixth's Circuit Court's decision to overturn the ban on affirmative action in public universities and government hiring is important in that some of the initiatives outlined above which have been enacted in other states will no longer be burdened. Government procurements are one of the main strategies for helping grow small businesses which will no longer be burdened by the ban on affirmative action.

Although helping minority-owned small businesses is important, it is not enough to simply voice the goal of doing so. We must strive to perfect policies such as those enacted in other states (outlined above) and implement similar policies and programs in order to kick start Michigan's economy. Minorities have become a powerful force to be recognized, especially within Michigan. Detroit's population, for example, is at an estimated 706,000, and the US Census Bureau (2012) reports that approximately 34% of that population are below the poverty level (US Census Bureau, 2012). This number shows that initiative must be taken in order to promote prosperity, and even more so in large urban areas such as Detroit where poverty is running rampant. In order to encourage the establishment and success of these businesses, Michigan needs to begin to consider implementing some of the policies which have been implemented by other states and private companies. Furthermore, there are other policies and procedures which can be followed or implemented in order to help grow Michigan's economy into a competitive market for small businesses.

Implementing Policies within Michigan Financing

Michigan would do well to implement an agency within state government which oversees the financing of small businesses and checks, especially, for discriminatory business practices

within the state. "African American and Latino business owners are more likely to be rejected on a commercial loan application than white businesses owners are, even when controlling for considerable demographic and business variables" (Lohrentz, 2010:363). These numbers compare to 18.5% of White male-owned businesses which, when starting a business, were able to gain access to the necessary financing, while less than 10% of minority owned businesses were able to do so (Lohrentz, 2010:363). These numbers are exacerbated by situations such as "lower inherited assets and lower savings rates among people of color and lower rates of property value accumulation in communities of color" (Lohrentz, 2010:364).

Implementing a process for procuring or financing an agency which oversees this process could help to make sure that minorities interested in businesses ownership have access to the capital that they need in order to establish their business and be successful. Virginia, for example, after spending less than 1% in those years at the turn of the century with minority-owned firms, implemented a voluntary program to help procurement within minority businesses. A similar program to assist minority owned firms could go a long way in helping minority owned businesses access the capital needed to establish their business.

Loan programs within the federal government can also be a way to promote the access of small businesses to sufficient capital. "State and local agencies can help fill the gaps in the commercial lending environment or play a major role in times of financial crisis" (Lohrentz, 2010:372).

Procurement Contracts

State and local labor contracts (procurements) can be a major source of revenues for new and start-up business (Lohrentz, 2010:372). These are generally done on a gender and race-neutral basis, however, there are variations which are more affirmative-action based (Lohrentz, 2010:372). "Contrary to the popular perception, affirmative procurement programs almost never involve set-asides where only minority or women-based enterprises are

allowed to bid on certain contracts" (Lohrentz, 2010:372).

Ensuring that government contracts in Michigan are directed or awarded to minority-owned small businesses can be a way for government to allow for greater success among minority-owned businesses in Michigan. This may also be implemented in regulating contractors to award a certain amount of sub-contracts to minorities-owned businesses. In overturning the ban on Affirmative Action, the Sixth Circuit Court has paved the way for a program such as this in Michigan. As was seen in Fullilove, City of Richmond, and Adarand, these are subject to strict scrutiny at a federal level, however, the Sixth Circuit has not implemented such a standard. Rather than set asides, these procurements are generally requirements that contractors utilize minority subcontractors, and government outreaches minority contractors to bid on government contracts (Lohrentz, 2010:372).

In order to promote this, a plan must be undertaken based on an assessment of disparities, as has been done at the federal level, which requires that several steps be taken. Depending on the specifics of the affirmative procurement program, a public agency may need to undertake a disparity or availability study to demonstrate the number and size of minority owned businesses within a specific industry that are ready, willing, and able to provide the proposed good or service. Generally, state and local governments must provide a higher level of evidence of specific disparities by place and industry than does the federal government (Lohrentz, 2010:364).


These steps must be taken carefully, however, as studies have shown that small businesses owned by minorities have a lower rate of success when they rely excessively on procurement programs provided by the state or local government and must diversify their revenues streams (Lohrentz, 2010:364). As a way to promote affirmative practices without creating set aside programs it is important to promote incorporation through outreach, social interaction, and networks between small

business owners within the Michigan business community.



Conclusion

Michigan's economy is already on the road to recovery. Recent efforts aimed at helping

small businesses to progress have already contributed to revitalizing the economy. By focusing more on small businesses, Michigan can improve its economy even more. The policies and programs discussed in this article are just a few of the many ways that states and local communities and businesses have taken to address the many barriers that disadvantage minority businesses. In the future, these approaches should continue to expand. Employing practices which help promote the success of minorities will help to close the wage gap and help minorities in small businesses to avoid the institutional biases which are so deeply embedded in our system. 

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